

ENTREPRENEURS & SITE GUIDES

MODULE 8: PRICING & FINANCIAL MANAGEMENT

INTRODUCTION

Sound financial management is essential for any business to be profitable. In this module, the participants will dive into the topics of pricing, budgeting and bookkeeping, using case studies of fictional companies.

Please note that this module requires some financial expertise from the facilitator. They can therefore bring in a guest lecturer for this module.

OVERVIEW



Learning Goals



Knowledge

- The participants will learn more about pricing, budgeting and bookkeeping and why these are important.



Attitude

- The participants will become more appreciative of financial management and bookkeeping.



Skills

- The participants will learn to analyze financial documents and how to use them for their own benefits.
- The participants will be able to come up with effective pricing strategies.

SESSION 8A: Pricing

SESSION 8B: Budgeting &
Bookkeeping

SESSION 8C: Cash Flow and
Profit & Loss Statements

BEFORE YOU START, YOU NEED...

- Flipcharts
- Large paper
- Marker and pens
- Sticky notes
- Projector



SESSION 8A: What Can I Do For You?

AGENDA



Discussion:
How Much Would
You Pay?
(30 min)



Lecture:
Pricing
Strategies
(30 min)



Exercise:
What Is a
Reasonable Price?
(30 min)

INSTRUCTIONS

Discussion: How Much Would You Pay? (30 min)



- Refer to a previous module where you looked at customer value.

Customer value can be expressed in terms of money: An entrepreneur will estimate what he/she thinks is the value of a product to its customers at a specific point in time. If he/she fails at this, the customer will either not buy the product or the entrepreneur might lose out on profits as the products are too cheap.



ASK:

- Ask a few volunteers to read out the following case studies. Ask all the participants to write down what they think would be the right price for the product. Ask them to write it in big symbols, so that you can read it from afar.
- After each case study, ask them to hold their prices up in the air and compare them. Ask a few participants to explain how they came to that price.

Case Studies:

- A) Lamasi Community Site is a small, but popular community tourism site in Somola. If you stay a night at Lamasi and choose to get the Lamasi Cultural Package, you will do a tour through the local community and the experienced guides will show you how to make the famous wooden Somo baskets, which you may take home after. At night you will enjoy a great traditional dinner where they will serve you up to 20 different dishes in a Somo basket! The famous Somo singers will come to sing their songs and play their flutes. The huts where you sleep are pretty luxurious, have nice beds and warm showers. Most importantly, the people are extremely welcoming and provide great service. What would you think is a reasonable price for the Lamasi Cultural Package per person?



- B) Your car is broken down and you are in the middle of nowhere in the extreme heat. Unfortunately you ran out of anything to drink and you are thirsty. You don't know how long you will have to remain here: a mechanic was coming your way but you have no idea how long it will take. But then, all of a sudden, a local shows up selling drinks. In fact, they are cold! You really want a bottle of water and you don't see any other trader! You know that normally you would pay 1,000 Ugx for a 500 ML bottle. The local, however, understands your need and decides to ask 30,000 Ugx for one bottle of water! You have the money with you, but you are shocked by the price. Will you buy it? Will you bargain? What is the maximum you will pay for it?
- C) In Natamba National Park, the chances of spotting the extremely rare and beautiful Bubu Bubu Bird are the highest in the world. Birders from all over the world come to Natamba National Park to see the Bubu Bubu Bird. The Natamba Wildlife Authority now offers full-day tracking activities where groups of max. 4 people are guided by 2 rangers to spot the bird. What do you think would be the right price per person for such an activity?
- D) Deep in the Dyeka forest, large deposits of petrified wood are found, which is ancient wood that because of pressure underground turned into some kind of stone over millions of years. For a piece the size of a chicken egg, you would typically pay up to \$15. However, there is a long tradition of petrified wood carving in Dyeka Village. It takes more than 5 years to learn this craft and only 3 people each year are allowed to start this costly training. As such, at this moment only 20 people worldwide know how to do it. At a local market stall in Dyeka Village you can buy a piece of authentic petrified wood that is beautifully carved into the shape of a crocodile. You hear that a skilled carver can craft such a piece in 8 hours. How much do you think would be a reasonable price for such a piece?



Lecture: Pricing Strategies (30 min)



SAY:

- Explain that, in order to get to a reasonable price, you have to take into account a number of factors:
 - Product characteristics:** How many/much of this product can you offer? If it is a service or activity it might be impossible to sell hundreds of them with a small team. Can you only sell it at specific moments or throughout the year? There are many other product characteristics that might influence your pricing.
 - Product costs:** This is a crucial factor. What does it cost you to produce or offer this product? Think of material costs, but also labour costs and overheads, etc.
 - The objectives of your company:** Is it your ambition to sell as many products as possible to everyone around? Or do you want to be more exclusive and make high profits on just a few sales?
 - Competitive situation:** Are you the only one who offers the product or do you have many competitors? At what price do other companies sell the product?
 - Demand for the product:** How popular is the product? Is it a luxury item or a bare necessity? How big is the market?



- f) **Customer's behaviour:** What customer segments do you focus on and what is their economic behaviour? Can they afford the product easily? At what moment and under what conditions do they buy the product?
- g) **Government regulations:** Sometimes products are heavily taxed by the government to discourage customers from buying them, such as with alcohol or cigarettes. It could also be that the government standardizes a price or offers subsidized competing products through their own institutions.



SAY:

- Maximizing your profit margins would be an obvious way to increase your profits. But increasing your prices might be counterproductive if it would mean that you lose customers because of it. Sometimes it might be better to lower your prices, to attract more customers.
- With all that in mind: how do you typically set the price for a given product? It really depends on the situation. There are a number of ways to do it:
 - a) **Cost-Plus Method:** this is the most common way small companies set their prices. They look at the costs they make, add a profit margin on top and that's the selling price. In other words: Total Cost (Fixed + Variable) + Profit = Selling Price. But this method doesn't look at the customer at all!
 - b) **Penetration Pricing:** this method is often used by companies that are new, quickly want to become known and are heavily competing with other companies to get the customer's loyalty. In this way, the company minimizes its prizes (and profits!) to outcompete other companies. Once they win the battle, they will increase the prices and make a profit. This is a method that is typical among food delivery and transport apps.
 - c) **Market Rate Policy:** This is often used if the products are similar to what competitors are offering. Think of non-perishable goods on the market, tailoring services or boda-boda or matatu transport. In this case, prices are fairly stable and customers expect to pay the same price every time.
 - d) **Variable Price Policy:** In this way, the price varies from customer to customer. There are several situations in which this could be beneficial. For example when you offer a discount for larger groups of customers, or when there are different customer segments with different paying abilities.
In the Ugandan tourism industry including national parks and many lodges, there are often different prices for East African Nationals and international tourists. This is largely based on the idea that the pockets of the average international traveler that can afford to come all the way to Uganda are bigger than those of the average local. But of course: this is definitely not always the case.
 - e) **Value-Based Pricing Method:** This refers to pricing based on exploring what their customer segments think it is worth. This can be done by simply asking the customers or by testing: change the price here and there and observe how potential customers respond to it.
 - f) Explain that in this training we believe it is important to familiarize oneself with the **Cost-Plus Method** and with **Value-Based Pricing**.

The participants might typically be familiar with the first method, but emphasize that you would like to encourage them to explore Value-Based Pricing. Typically you would want the price that you get through the Cost-Plus Method to be lower or the same as the one through the Value-Based Pricing Method. If the former is lower, it means that you can increase your profit margins and customers will still buy it. If the Cost-Plus Method leads to higher prices than what the customer believes it is worth, the business potential of the product is lacking!



Lecture: Pricing Strategies (30 min)



- Introduce the fictional company of John Bosco:

"Hello everyone, my name is John Bosco and together with my friend Charles, I started a company about two years ago called Gulu-a-Gogo. We offer Boda-Boda tours in Gulu and the wider Acholi region. We really believe that Boda-Boda tours are a great way to let both international and domestic tourists experience the cultural and natural splendour of Northern Uganda! Next to Charles and myself, the company employs 2 staff members, who take care of the marketing and administrative matters. Charles and I like to do the guiding ourselves! We have a small office at one of the co-working spaces in Gulu. Currently the boda-bodas are rented through a company called Acholease."

- Explain to the participants that they are now going to look at the pricing of Gulu-a-Gogo and that they are going to explore what would be a reasonable price to charge, using both the Cost-Plus Method and the Value-Based Pricing Method.

Below are the costs that the company makes. The company has asked some potential customers what the maximum price they would be willing to pay for the tour is.

Cost-Plus Method	Value-Based Pricing Method
Staff Salaries: \$15	Person 1: \$80
Boda-Boda rent and petrol: \$15	Person 2: \$40
Lunch: \$5	Person 3: \$85
Office rent: \$10	Person 4: \$200
Other fixed costs: \$5	Person 5: \$80
Total costs: \$50	Person 6: \$95
20 % Profit = 20% of \$50 = \$10	Person 7: \$120
Price = \$60	Average = \$100, Price = ?

- In the example above, the Cost-Plus Method led to a price of \$60. If the company charges \$60, 6 out of 7 customers would buy it. But it looks like a cheap price compared to what the customers want to pay!
- In the case of the Value-Based Pricing Method, the average response of potential customers was that they would be willing to pay \$100. Does that mean \$100 is the right price? Probably not, as only 2 of the customers would actually buy it! That is why it would not be a good idea to look at the average, but to look at a number that many potential customers would be willing to pay.

In the table below you can see what is the right pricing:



Price	No. of Customers	Total Turnover	Total Costs	Total Profit
\$40	7	\$280	\$350	\$-70
\$60	6	\$360	\$300	\$60
\$80	6	\$480	\$300	\$180
\$85	4	\$340	\$200	\$140
\$95	3	\$285	\$150	\$135
\$100	2	\$200	\$100	\$100
\$120	2	\$240	\$100	\$140
\$200	1	\$200	\$50	\$150

- In this example, it shows that charging \$80 would result in the highest profits, of \$180, whereas the Cost-Plus Method of \$60 only led to a profit of \$60. Even charging \$200, which is a price that most people would think is outrageous, would lead to a higher profit.
- However, in this example we are making one bold simplification: it appears that the costs remain stable, regardless of how much you sell. This is obviously not true in the real world: if you have an office, your landlord will not be bothered at all with your profits: the landlord will just want you to pay your rent. The more you sell, the smaller the percentage of each sale goes to paying your office rent. Normally the costs per item decrease when you sell more products, as the fixed costs form a smaller part of the costs.
- All in all, it is fair to say that \$80 would be a reasonable price for Gulu-a-Gogo's Boda-Boda Tour.
- The participants will now apply this exercise in a different case: the cost of a traditional Acholi lunch that can be bought additionally on a trip.

What would be the best price to sell these lunches for?

Maximum price that potential customers want to pay for a traditional Acholi lunch.

Person 1: \$10

Person 2: \$10

Person 3: \$20

Person 4: \$15

Person 5: \$5

Person 6: \$3

Person 7: \$12

Best Price = ?

Cost are \$5 per lunch



Fill in this form to find out the right price.

Price	No. of Customers	Total Turnover	Total Costs	Total Profit

Correct answer:

Price	No. of Customers	Total Turnover	Total Costs	Total Profit
\$3	7	\$21	\$35	\$14
\$5	6	\$30	\$30	\$0
\$10	5	\$50	\$25	\$25
\$12	3	\$36	\$15	\$21
\$15	1	\$15	\$5	\$10
\$20	1	\$15	\$5	\$10

The profit is highest at a price of \$10 per lunch, so \$10 would be the right price for the lunch.



SESSION 8B: Budgeting and Bookkeeping

AGENDA



Lecture:
Introduction
into Financial
Management
(15 min)



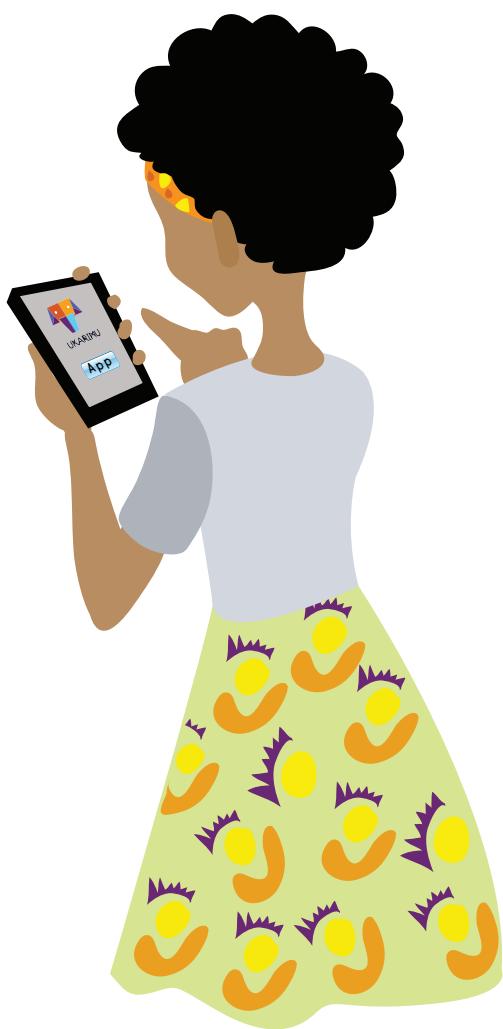
Exercise:
Budgeting
(45 min)



Lecture:
Bookkeeping
(15 min)



Exercise:
Bookkeeping
(45 min)



Lecture: Introduction into Financial Management (30 min)



ASK:

- Ask the group split up in small groups of 2 to 3 people and discuss the following questions: How would they describe financial management. What does it entail? Why is it important? Do they like it? Who is the one in charge of it at their company?



ASK:

- Ask the group if there are any specific things they would like to learn when it comes to financial management and write them down on a flipchart. Make sure to try and answer most of them throughout the day, or if you are unable to answer questions yourself: make sure to help the participants to find the answer.



SAY:

- Explain: Financial management includes bookkeeping, projections, financial statements and financing which forms the foundation for reaching any entrepreneur's goals through sound business decisions.



SAY:

- Explain: Financial management is the way to know if the business is making a profit. Financial management helps the business to decide what it can afford in terms of store or office location, inventory purchases, employees, and equipment. You need sound financial information to set your prices and select your vendors. Financial management gives you the tools to plan for overall business growth, for diversification of your product lines, or for reaching new markets. Financial management helps you decide which products, services, and markets are profitable. Effective financial management gives you tools to chart your course into the future, adjust your direction when needed, and help you find your way through challenging times.



SAY:

- Explain: If the business' growth requires financing (loans), financial management provides the information to know how much you can afford to borrow for your business. Financial management gives you not only the documentation needed for a loan application, but also helps you discuss your business circumstances with a lender in terms that improve your ability to qualify for the loan.

INSTRUCTIONS



Exercise: Budgeting (30 min)



SAY:

- Creating a budget is the first place to start with your financial management practice. A budget is a financial plan that details the projections on Incomes and expenditures on a short or long term basis. A budget is a tool that helps you:



- a) Track all business expenses
- b) Plan for the future i.e. the most efficient way to spend your projected incomes.
- c) Economize when you need to
- d) Plan for expansion
- e) Make a profit

Once you create a budget, use it to compare what you've budgeted with your actual income and expenditures.

- Show this sample budget list, which covers most typical business budget lines. If any of the budget lines are unclear, elaborate on them.

Category	Monthly Budget	Actual Expenditure
Incomes		
Income source 1		
Income source 2		
Total Income		
Expenditures		
Rent		
Utilities		
Telephone & Internet		
Insurance		
Employees or Contractors		
Office Supplies		
Inventory Purchases		
Permits & Licenses		
Travel		
Interest		
Bank Service Charges		
Postage		
Legal & Accounting		
Other		
Total Expenditures		
Surplus/(Deficit)		





ASK:

- Ask the group to split up in groups of 3 and create a budget for Gulu-a-Gogo. Provide them the following information:
 - a) The most reasonable price is charged for Gulu-a-Gogo's Tour Services as seen in the above pricing methods. They generally have 30-50 customers per month.
 - b) Think of a possible second income stream that Gulu-a-Gogo could have at a rate of 1,000,000 Ugx per month.
 - c) The marketing employee earns 400,000 Ugx per month, the administrative employee 400,000 Ugx per month.
 - d) Their office rent is 12,000,000 per year.
 - e) They provide travel expenses of 5,000 Ugx per staff member per day. They also provide simple lunches for their staff.
 - f) They are fully insured at a Premium of 4,500,000 Ugx per year, registered with UTB at a one-time cost of UGX 200,000 and have an Equity bank account which charges aggregated bank charges of UGX 80,000 per month.
 - g) At Acholease, they can rent good Boda-Bodas for 25,000 Ugx per day, but they spend money on petrol as well.



Lecture: Bookkeeping (30 min)

- Explain that bookkeeping is the organized process of tracking all income and expense transactions. Bookkeeping is a critical component of financial management, which leads to better business decisions regarding financing, taxes, owner's draw, and retirement. Here are some basic bookkeeping steps:
 - a) Obtain business accounting software. Proper software selection is critical for success.
 - b) Open a separate business checking account. Do not mix business and personal checking accounts.
 - c) Reconcile your bank account. Each month, reconcile your account using business accounting software.
 - d) Track sales. Create an airtight system for tracking sales using tools such as invoices, and a sales book. Always use this sales tracking system.
 - e) Deposit all sales. Using the duplicating deposit slips, deposit all sales in your business bank account. Total sales should equal total deposits. Do not spend cash sales. Link all forms of sales documentation (such as invoices, and sales books) with a specific deposit.
 - f) Document all business expenses.
 - g) Run a profit and loss (P&L) statement. A checking account balance is not a good indication of how much profit the business has made or what amount is available for the owner's draw. A P&L statement can provide a better picture of the financial health of the organization.



Exercise: Bookkeeping (30 min)



ASK:

Ask the same groups of 3 to prepare the necessary supporting documents that the company should put in place with the additional information below:

- On (state past date), the company provided Tour Services to Michelle (a customer/client) and her 3 friends. Michelle paid up \$240 for the services fully in cash on the same day.
A Sales Receipt should be issued in this case. Look out for these critical items:
 - a) Name and Company details
 - b) Title of the document - “Sales Receipt”
 - c) Date
 - d) Customer Name/Details
 - e) Type of Service offered
 - f) Amount paid and method of payment (Cash).
 - g) Balance (Nil)
 - h) Signature of issuing officer
- On (state past date), the company wanted to procure the following items for the upcoming week. Since some suppliers do not issue proper documents, the company resorted to using Payment Vouchers that are used to record such expenditures. Request the team to come up with a Payment Voucher for the following expenditures.
 - a) The company was to buy 3 reams of paper at Ugx 20,000 each
 - b) The company wanted to pay their Fuel bill at Gulu Fuels (a local fuel station) of Ugx 245,000
 - c) They also planned to buy jackets for 6 of their riders at a rate of Ugx 40,000 per jacket.
 - d) Pay for their Internet costs of Ugx 300,000 for the previous 2 months.
- A Payment Voucher should be issued in this case. Look out for these critical items:
 - a) Name and Company Details
 - b) Title of Document (Payment Voucher)
 - c) Date
 - d) All expenses with Unit Price, Units and Amount fields
 - e) Total Amount
 - f) Sign off by Preparing Officer



SESSION 8C: Cash Flow and Profit & Loss Statements

AGENDA



Lecture:
Cash Flow

(15 min)



Exercise:
Cash Flow Statement

(15 min)



Lecture:
Profit & Loss Statement

(30min)



Summary:
Five Key Points to Remember

(10 min)

Lecture: Cash Flow (15 min)



SAY:
Give the following lecture:



- *Cash flow can be defined two ways:*
 - a) Balance of cash received less the amount of cash paid out over a period of time*
 - b) Moving cash in or out of a business*
- *A cash flow projection is a financial statement that tries to show how cash is expected to flow in and out of a business over a future period of time. A cash flow projection is used to see if projected cash receipts (in flows) will be sufficient to cover projected cash disbursements (out flows). A business can be profitable and still run out of cash. As an investment banker might say, “Cash flow projections provide the visibility needed to avoid liquidity problems.” In other words, a cash flow projection is a tool to help you manage your cash so you can pay your bills on a timely basis and keep the doors of your business open.*
- *A cash flow projection is a great tool for setting sales goals and for planning for expenses to support those sales. A related use of a projection is to determine your break even point during a start-up or expansion phase. If you need to plan for a large expenditure, such as an equipment purchase or move to a new location, a cash flow projection is the perfect tool. Similarly, if you have a seasonal business with large inventory purchases, a projection can help you have the cash on hand to make a large inventory investment when you need it.*
- *A P&L statement can mask cash shortages if you use accrual accounting. A cash flow projection helps you see the cash status of your business now and plan into the future. A cash flow projection is a good way to prepare and plan for your financing needs and is often a required part of a business loan application.*



INSTRUCTIONS



Exercise: Cash Flow Statement (30 min)

- Give the same groups of 3 the following overview of a Cash Flow Statement of Gulu-a-Gogo.



SAY:

- The company has prepared the cash flow statement below for the recently concluded year in business and it looks as follows.*

INFLOWS	UGX
Tour Services Income	24,600,000
Sale of Gulu-a-Gogo Shirts and Caps	8,500,000
TOTAL INFLOWS	33,100,000
OUTFLOWS	
Rent	9,000,000
Salaries	2,500,000
Entertainment	11,500,000
Utilities	2,500,000
Fuel	4,800,000
Printing and Stationery	1,200,000
Cost of Shirts and Caps Sold	10,000,000
Internet Costs	2,000,000
TOTAL OUTFLOWS	43,500,000
NET CASH FLOWS	(10,400,000)

The company is in a huge deficit which shows that it is spending way more than its earnings. An urgent intervention is required in order for the company to survive.



ASK:

- Ask the participants to reflect on what should be done and let them think how the company should change.



FACILITATOR'S TIP:

- That the company is spending quite a lot on the Entertainment. The company should be able to significantly reduce this expenditure in order to improve its cash flow position.
- That the company is only making losses on the sale of Shirts and Caps. This is a product that the company can do away with in order to improve its cash flow position.



Lecture: Profit & Loss Statement (20 min)



Give the following lecture about the Profit & Loss Statement:



- *The P&L statement is the best tool for knowing if your business is profitable. A P&L statement measures revenue (also called sales or income) and expenses over a month, quarter or year. With it you know if you have made a profit (and how much) or if you have incurred a loss.*
- *The most important financial management report is the P&L statement. A P&L statement will reflect your business decisions on the basic buying and selling process. A P&L will tell you how well you are managing your business and provide information on how to grow your business.*
- Basic Formula for P&L Statement

$$\text{Sales} - \text{Cost of Goods Sold} = \text{Gross Profits} - \text{Overhead} = \text{Net Profit}$$

Sales (also called Income or Revenue): Total amount from selling your product or service during a certain time period.

Cost of Goods Sold: Total expenditure for inventory items which customers buy. Cost of Goods Sold consists of the cost of purchasing the items, freight, manufacturing costs, modification costs, and packaging. For services, this is the cost of providing the services, including labor, material used, and transportation.

Gross Profit: Sales less Cost of Goods Sold.

Overhead: Expenses associated with your ongoing business operation, such as rent or utilities.

Net Profit: Gross Profit less Overhead. Net Profit is what remains to pay for expansion, equipment, loan repayment, income taxes and owner's draw.

- Compiling a P&L Statement

All quality business accounting software programs compile a P&L statement at the push of a button. The accuracy of your P&L statement will depend on how it is set up for your company and your input data. Print out your P&L regularly to track your business progress. Use your P&L statement as the basis for building a cash flow projection.



Summary: Five Key Points to Remember (20 min)



- Start financial management with a budget.
- Sound bookkeeping is the basis for all financial management.
- Cash flow projections will help you to see cash shortages.
- A Profit & Loss (P&L) statement is the best tool for knowing if your business is profitable.
- Financing is getting the money you need to start, operate or grow your business. Before borrowing money for your business, develop a business plan to help determine whether your business can afford a loan. If you need to borrow money, take time to comparison-shop for the best loan option.

